

## **The Aftermath of International Taxation Laws on Indian Economy: an Overview on Transfer Pricing**

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**ABSTRACT:** *The major two words GLOBALIZATION AND MODERNIZATION have made a huge impact on the world economy. As we set out toward globalization and modernization, we are moving towards exhibiting the dynamic and moldable arrangement of world. The world has turned out to be an open market because of which global speculation and cross outskirt business have turned out to be the fundamental piece of our new world. With respect to India, Indian government has opened up its market and welcomed several multinational companies to bloom its business in India. Almost certainly because of this, FDI inflow and speculation has elevated Indian GDP. Within all this gigantic development, the key inquiry that remains is how much tax Indian government is gathering as a byproduct of enabling Multinational Corporation to work here in India. Has India been successful to set up an international taxation framework so as to influence business to work easily and in the meantime charge appropriate tax on those organizations?*

**KEYWORDS:** *Foreign Direct Investments, Gross Domestic Product, Safe Harbour Rules, OECD Guidelines, Economy.*

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### **I. INTRODUCTION**

#### **International Taxation**

International taxation is the study or calculation of tax liability of an individual or business with respect to the tax laws of various countries or the international aspects of an individual country's tax laws as per the situation.

#### **Transfer Pricing**

Transfer pricing is the setting of the price for transaction taken place between controlled (or related) legal entities inside an undertaking. For instance, if a subsidiary organization provide some service to a parent organization, the expense borne or paid by the parent to the subsidiary is the transfer pricing. Legal entities considered under the control of a sole enterprise includes branches and organizations that are entirely or majority shares are claimed at last by the parent company.

Overall this makes a tremendous chain of mistrust between tax authorities and MNC's which hampers FDI inflow and economy. So, to handle such issue, a few solid steps have been taken by Indian government. Few are as below:

**Safe Harbour Rules:** In order to reduce the number of transfer pricing audits, cases and disputes, a new section 92CB was introduced in Income Tax Act, 1961 to provide that the calculation of arm's length price under section 92C or section 92CA will be subject to Safe Harbour rules. A safe harbor is a provision of a rule or a regulation that determines that specific conduct or action done does not violate a given guideline or rules. Whereas, "unsafe harbors" portray direct that it will be in regard to damage the rules, regulations and law.

**Advance Pricing Agreements:** An Advance Pricing Agreement is an agreement, for the number of years, between a tax payer and one tax authorities indicating the pricing techniques that the tax payer will apply to its related-company transaction. These projects are intended to help tax payers resolve genuine or potential transfer pricing question in a proactive, agreeable way, as an option to the conventional examination process.

#### **Advance Ruling**

The provisions of advance rulings were presented under the Finance Act, 1993, Chapter XIX-B of the Income Tax Act, 1961 deals with advance rulings, came into power with effect from 1<sup>st</sup> June 1993. Under this chapter power of giving advance rulings has been appointed to an autonomous adjudicatory body. Which is a

high-level body consisted of retired judges from Supreme Court and high court and now engaged in issuing advance rulings. The provisions recommended were simple, modest, fast and authoritative.

□ **Organisation For Economic Co-Operation And Development (Oecd)**

The Organization for Economic Co-operation and Development (OECD) is basically a monitoring authority and research and decision-making organization. OECD was created with the motive of cultivating economic development and cooperation among the countries related to international transaction, also fighting poverty and ensuring the environmental impact of growth and social development. It has faced a wide range of issues, including raising the standard of living in its member nation, adding to the expansion of world transaction and promoting economic stability.

□ **Arms Length Pricing**

The provisions of Transfer Pricing have been introduced to ensure that income arising from an international Transaction between Associated Enterprises shall be computed having regard to the Arm's Length Price. Any cost or expense allocated or apportioned between two or more associated enterprises under a mutual agreement or arrangement shall also be at an Arm's Length Price. The arm's length price in relation to Transfer Pricing in an international transaction shall be determined by any of the following Transfer Pricing Methods

- Comparable Uncontrolled Price Method
- Resale Price Method
- Cost Plus Method
- Profit Split Method

## **II. REVIEW OF LITERATURE**

1. (Cravens, 1997) Rather than a purely-tax driven mechanism, international transfer pricing can be considered as a way to achieve corporate goals and in this way make key outcomes. This paper looks at the consequences of an overview of administrators of US-based worldwide firms who portray their international transfer pricing objectives and strategies of their organization results demonstrate that administrators are not exclusively centered around tax assessment issues as the essential goal of international transfer pricing estimates multi-nationals utilize transfer pricing to help them accomplishing upper hand and other corporate targets too
2. (Lakhal, 2006) This research paper helps us in understanding the relationship between an operational profit sharing and transfer pricing for network manufacturing companies new age organizations are fashioning associations with different firms to advertise items that have been gathered through assembling exercises dispersed at various areas. These areas have place with more than one organization and the item goes through these distinctive locales amid its assembling stages. This assembling joint effort is known as system producing. As per the system theory organization frame unions to make an item and offer in its working benefits.
3. (Oyelere& Emmanuel, 1998)- The potential utilization of transfer pricing as a profit shifting system by Multinational Corporation has been recognized. In any case, there is generally little proof to substantiate or limit this case in connection to UK-based foreign controlled ventures. This paper analyzes the conceivable utilization of Transfer Pricing as a profit shifting component by multinational companies operating in the UK. The paper includes the examination of the profitability and dividend distribution of few of foreign-controlled ventures with those of UK-controlled ventures over a two-year time span..
4. (Grantley & Grant, 2012)- This paper studies at the international corporate tax avoidance practices of listed Australian firms. In view of a few example of 203 listed Australian firms over the 2006–2009 period (812 firm-years), results demonstrate that there are a few practices Australian firms use to forcefully lessen their tax liabilities. In particular, paper locates that thin capitalization, transfer pricing, profit shifting, multi-nationality, and tax haven are used for tax avoidance.
5. (Lohse & Riedel, 2012)- Over the past decade, several countries augmented their national tax law by means of transfer pricing legislation with a purpose to restrict opportunities for tax-stimulated transfer price distortions and the related relocation of multinational income from their borders. This paper empirically inspects the impact of transfer pricing legal guidelines on multinational profit shifting behavior. Particular records on the evolution of country wide transfer price requirements in Europe over the past decade. These statistics is connected to accounting facts on multinational companies in the EU and to corporate tax fee information.

### III. RESEARCH DESIGN

#### □ **Objective Of Research**

To study and analyse the effect of International Taxation Norms with respect to its potency on the Indian Economy. Our primary motive is to identify the requirements, necessity, and challenges of such International Tax Laws in India and to analyse them along with several case studies and with references from other research scholars.

#### □ **Type Of Research**

The type of research that will be used in this study is qualitative research and quantitative research. Qualitative researchers aim to gather an in-depth understanding of secureness and safety of the International Tax Laws which are applicable to the Nation.

#### □ **Data Sources**

The amendment on India's new international taxation standardization has been obtained from various reports from Ernst & Young, Deloitte & KPMG. The data on various Macroeconomic factors & FDI inflows were collected from the budget documents of RBI and the Department of Revenue, Government of India.

#### □ **Sampling Method**

The research sampling method that will be used in this study is random sampling technique. By using this technique, we believe we would end at a more realistic result that could be used to represent the major essence of the topic

#### □ **Statistical & Analytical Tools**

For the purpose of analyzing the sample data collected we have used several analytical and statistical tools such as Percentage Method etc. with the help of software's like MS-Word, MS-Excel.

### IV. DATA ANALYSIS

#### **Vodafone Tele-Services (India) Holdings Ltd Vs Union Of India (Bombay High Court)**

Introduction to the case

- Vodafone India Services Ltd. is a subsidiary of Vodafone Tele-Services (India) Holdings Ltd., which in turn is a non-Indian company. Vodafone Holding is an AE (Associate Enterprise) of Vodafone India with the end goal of exchange estimating arrangements under section X of Income Tax Act 1961. Vodafone India is occupied with giving administration in connection to telecommunication in India.

Facts of the Case

- During the AY 2009-10, Vodafone India issue equity share to Vodafone Holding at premium and the same is mentioned in 3CEB in tax audit report. The issue of share is as follows: -

Total No. of Equity Share –	289224
Face Value per Share –	Rs. 10
Premium per share –	Rs. 8509
Total Issue Price –	Rs. 8519
Total Consideration Received –	Rs. 246.38Cr.

- Vodafone India declared the share issue to be an international transaction and also declares that the income of the petitioner was not affected with such a transaction in FORM 3CEB.

Vodafone's reasoning before the Assessing Officer/Transfer Pricing Officer

- Vodafone argued that transfer pricing cannot be applicable to such transactions as Chapter X of Income Tax Act 1961 is not pertinent to transactions involving issue of shares as no income is being affected by issue of shares.
- The Transfer Pricing Officer (TPO) asserts that that the issue is at a cost/price below the equitable market value and subsequently has brought about the advantage to the Associate Enterprise, in view of which the Assessing Officer ('AO') finished the Assessment The dispute resolution panel constituted by the Central Board of Direct Taxes manifested that the Assessing Officer had the jurisdiction to invoke the provisions of transfer pricing in the case of issue of shares at a price below the fair market value. The TPO sums up to an arm's length price of Rs. 1555cr, and then passed an assessment order for the difference of Rs. 1555-Rs. 246 = Rs. 1308cr. The amount was then assumed to be a deemed loan to the associate enterprise and was asked to calculate an interest of 13.5% on the deemed loan. The total adjustment for transfer pricing was at the hands of Vodafone India which summed up to Rs. 1397cr.

Appeal at the High Court

- Vodafone India challenged the final interpretation of AO at the high court stating that Section X of Income Tax Act, 1961 is not applicable on issue of equity shares to the holding organization or company.

After going through the above said facts, Mr. Harish Salve, a learned Senior Counsel appearing in support of the Petition states that: -

- Chapter X of the Act are special provisions relating to avoidance of tax. Section 92 of the Act provides for arriving at income arising from International Transaction, having regard to Arm's length price. Section 92(1) of the Act which applies to the present facts, directs that any income arising from an International Transaction should be computed, having regard to the ALP. Thus, an essential condition, for application of Section 92(1) of the Act is that income should arise from an International Transaction. In this case, it is submitted that no income arises from issue of equity shares by the Petitioner to its holding company.
- The issue of shares by the Petitioner to its holding company and receipt of consideration of the same is a capital receipt under the Act. Capital receipts cannot be brought to tax unless expressly brought to tax by the Act. It is well settled that capital receipts do not come within the purview of the word 'Income' under the Act, when so expressly provided as in the case of Section 2 (24) (vi) of the Act. This brings capital gains chargeable under Section 45 of the Act.

The Final Judgment

- Along these lines to get over exchange mis-estimating/control/misuse that the market-based exchange valuing was presented, known as ALP. Along these lines, unmistakably Chapter X of the Act currently existing was to guarantee that qua International Transaction between AEs, the benefits are not downplayed nor misfortunes exaggerated by maltreatment of either demonstrating lesser thought or higher costs between AEs than would be the thought between two autonomous substances, uninfluenced by relationship. It didn't supplant the idea of Income or Expenditure as typically comprehended in the Act for the reasons for Chapter X of the Act.

### Gdp Growth In India

The Gross Domestic Product of our country has always been growing at a positive pace, mainly due to the FDI inflows in the country.

YEAR	GROSS DOMESTIC PRODUCT IN BILLION USD
2013-2014	1863.21
2014-2015	2042.44
2015-2016	2095.40
2016-2017	2274.20
2017-2018	2602.31

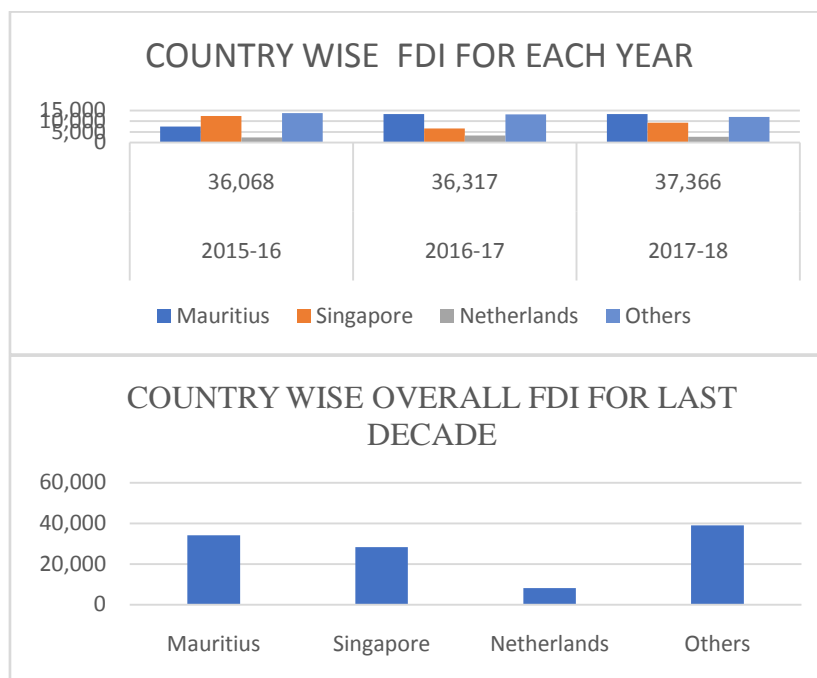
### Foreign Direct Investment In India

YEAR	FDI in billion USD
2013-2014	16.05
2014-2015	24.75
2015-2016	36.07
2016-2017	36.32
2017-2018	37.37

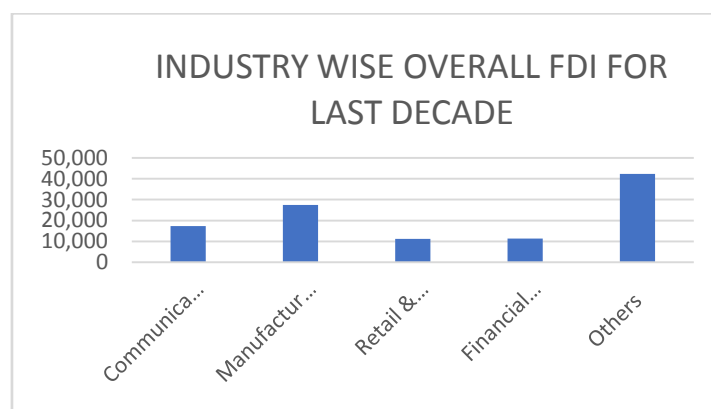
From the above data of foreign direct investment, we can say that there is no constant increase or decrease in the inflow of foreign investment.

ALL DATA IS IN MILLION \$

Source/ Industry	2015-16	2016-17	2017-18	TOTAL
Total FDI	36,068	36,317	37,366	109,751
<b>Country-Wise Inflows</b>				
Mauritius	7,452	13,383	13,415	34,250
Singapore	12,479	6,529	9,273	28,281
Netherlands	2,330	3,234	2,677	8,241
Others	13,807	13,171	12,001	38,979
<b>Sector-wise Inflows</b>				
Communication Services	2,638	5,876	8,809	17,323
Manufacturing	8,439	11,972	7,066	27,477
Retail & Wholesale Trade	3,998	2,771	4,478	11,247
Financial Services	3,547	3,732	4,070	11,349
Others	17446	11966	12943	42,355



From the graphs, it can be easily concluded that the foreign direct investment over the last ten years, are basically from countries like Mauritius, Singapore, Netherlands, USA and Japan to a few major sectors only, which is because of the double taxation avoidance agreements and treaties with those countries and India.



#### THE TRANSFER PRICING COURT LITIGATION TRENDS IN OUR COUNTRY

Indian Courts (including the Tribunal) have delivered over 2500 TP rulings till date. During FY 2014-15, the number of rulings undertaken shows an increase of over 40%, when compared with the earlier FY. The current TP litigation trend exhibits that majority of the rulings are being pronounced at the Tribunal level, which is known to be the final authority for finding out facts and figures of the cases undertaken

FORUM	No. Of CASES (FY 2014-2015)
Supreme Court	4
High Court	41
ITAT	486
TOTAL	531

#### V. FINDINGS AND SUGGESTIONS

The main intention behind the research is to understand the position of the Indian economy with regard to the international taxation laws and also to know how the foreign direct investments have an impact on the gross domestic product of our country. This examination has kept a simplified & overall approach to view the International taxation amendments, relationships & improvements. With new changes in the international tax laws such as the safe harbor rules etc. have had an impact on the FDI's. It has also led to an elevation helping multinational companies to bring in more investments.

□ **Dispute Resolution Panel (Drp)**

In the year 2009, the Government of India came up with a new dispute resolution mechanism called the dispute resolution panel (DRP). From the above data analysis it is evident initially, with such a mechanism the settlement of transfer pricing cases has happened faster.

□ **The Relationship Between Variables**

From this examination we are seeking to locate the different laws on international tax collection that has been conveyed to have an impact in India and endeavor to build up a nexus between the new International tax that has been actualized or implemented, FDI inflows that is coming in India, corporate Tax Revenue gathered and Gross Domestic Product of India.

□ **Unpredictability Of General Anti Avoidance Rule (Gaar)**

The dominant focus of the Government of India has been to exercise a revision on its laws to discourage illegitimate tax planning. As part of this plan, GAAR came into effect from April 1 2017. The rule will empower the Indian tax authorities to scrutinize investment structures & other transactions. Hence, investments made in India through a third-party country need to pass the test of GAAR before receiving a tax benefit under the double taxation agreement.

□ **Tribunal Hearings In Favor Of The Tax Payers And Delay In Settlements**

Tribunals had delivered 486 rulings, of which 57 were to stay on demand. In the balance 429 cases (dealing with substantive issues), 292 cases (69%) were in favor of taxpayers, whilst only 21 cases (i.e. less than 10%) were concluded in favor of the revenue authorities. In the balance cases, the various appellate grounds have been ruled partly in favor of the taxpayer and partly in favor of revenue authorities

□ **Implementation Of Safe Harbour Rules And Advance Pricing Agreements**

One of the major problems that India was facing was no clear & transparent International law. One of the aspects of International tax law is International Transfer pricing. The Comptroller and Auditor General of India, in his recent report on direct taxes, estimated that nearly US\$50 billion was tied up in appeal cases in 2009–10. A further US\$20 billion was locked up in appeals at higher levels. The report suggests India is growing with several implicit losses. In order to resolve such issues, Safe Harbour Rules & Advance Pricing Agreements have been brought into action.

## VI. CONCLUSION

We see consistent changes and moves in economy happening each day yet one of the imperative angles for government to work is its economy, where tax is gathered from the individual, households and organizations. As we are aware of the major goal of tax gathering is for the nation's welfare and the defense framework of the country which can't be overlooked at any cost. In addition, globalization is at its peak making more complex and dynamic tax norms.

With globalization, and inter border trade practices, the government of India has been increasing its effort to provide the investors with an ease of tax regime. This has led to India signing many agreements with regard to double taxation. These agreements not only see to that the income is being taxed twice or not, but also promote trade which in turn benefits the Indian economy.

Yes, the changes in the international tax norms have added to the development of Indian Economy. Bringing in Safe Harbour Rules, have in fact added on to the number of FDI's entering our country. But the question that is yet to be answered is the inefficiency of the tax authorities in settling the Transfer Pricing cases in India. Though mechanisms such as Dispute Resolution Panel (DRP) were introduced, it did not succeed because of the negligence in settling the cases. The main intention of setting up such panels were wrecked.

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